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ADMINISTRATIVE AND BUDGETARY COORDINATION OF THE UNITED NATIONS WITH THE SPECIALIZED AGENCIES AND THE INTERNATIONAL ATOMIC ENERGY AGENCY

Note by the Secretary-General

The Secretary-General has the honour to transmit to the members of the General Assembly the interim study on the need for the development of accounting standards to be applied in the United Nations system, prepared by the Panel of External Auditors in accordance with General Assembly resolution 45/235 of 21 December 1990.

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* A/46/150.

Letter of transmittal

Sir,

I have the honour to transmit to you, in accordance with the request by the General Assembly in paragraph 5 of resolution 45/235 of 21 December 1990, the interim study by the Panel of External Auditors of the United Nations, the specialized agencies and the International Atomic Energy Agency on the need for the development of accounting standards to be applied in the United Nations system.

Accept, Sir, the assurances of my highest consideration.

(Signed) John BOURN
Comptroller and Auditor General of the
United Kingdom
and
Chairman, Panel of External Auditors

The Secretary-General of the United Nations
New York, N.Y.

Interim study on the need for the development of accounting standards to be applied in the United Nations system

I. INTRODUCTION

1. As a result of a meeting between the Advisory Committee on Administrative and Budgetary Questions (ACABQ) and the Panel of External Auditors, at which the question of the development of generally accepted accounting principles to be applied by United Nations organizations was discussed, the ACABQ recommended that the General Assembly request the Panel of External Auditors to commission a study for the development of generally accepted accounting principles and standards for consistent application in the United Nations system. Subsequently, the Assembly, in paragraph 5 of its resolution 45/235, requested the Panel to:

> "Submit to the General Assembly at its forty-sixth session, through the Administrative Committee on Coordination and the Advisory Committee on Administrative and Budgetary Questions, an interim study on concrete issues to be resolved through the development of appropriate accounting principles and standards for consistent application in the United Nations system, taking into account the feasibility and benefits of such principles, as well as the major problems to be addressed in this regard".

2. The present paper and its annexes I and II set out the Panel's consideration of the issues involved, the benefits that will accrue, the problems to be resolved and the feasibility of the proposals. Annex I develops further the points covered in this paper following a request by the Consultative Committee on Administrative Questions (Financial and Budgetary Questions) (CCAQ (FB)) at its seventy-fourth session in March 1991 that the Panel provide an elaboration of its interim study for the seventy-fifth session of CCAQ (FB), to be held in September 1991. Annex II outlines in more detail the benefits that, in the opinion of the Panel, would derive from the application of several international accounting standards to United Nations organizations.

II. THE ISSUES

3. According to paragraph 6 (b) (v) of the annex to the Financial Regulations of the United Nations, the auditor's report should mention deviations of a material nature from generally accepted accounting principles. This requirement has been reflected in paragraph 17 (d) of the common auditing standards adopted by the Panel of External Auditors. However, there is no definition of what constitutes "generally accepted accounting principles" within the United Nations system; nor in practice is there a common set of accounting principles and standards, or even a common interpretation of accounting terminology, being consistently applied either between organizations or, in some cases, within the same organization.

4. The absence of a set of accounting standards common to the United Nations system has led to differences in such matters as the consistent accounting treatment of material transactions and in the levels of their disclosure. The Panel believes that these factors have caused Member States and other users of the accounts, including potential donors, difficulties in the interpretation of the financial statements and in making comparisons between one United Nations organization and another.

5. Furthermore, the lack of common standards has created particular problems for external auditors, and on several occasions there have been disagreements between auditors and the officials of the audited organizations on the proper treatment of a material item in the accounts, either because of a variation between two series of standards or the absence of a clear standard to be applied in the particular case.

III. BENEFITS OF COMMON ACCOUNTING STANDARDS

6. In the Panel's view, the consistent application of generally accepted accounting standards would improve the fair presentation of the financial position of the organizations and the results of their operations. This would ensure that the readers of the accounts, in particular Member States and potential donors, would be more properly and clearly informed. The general use of such standards would also allow Member States and other users to make meaningful comparisons of the performance of the respective organizations.

7. An agreed set of common accounting standards would allow organizations to clarify the accounting procedures set out in their financial regulations and rules and enhance understanding between organizations when activities are funded and carried out on an inter-agency basis. The standards would also facilitate the task of the administration in fulfilling General Assembly resolution 44/183, in which the Secretary-General and the executive heads of United Nations organizations and programmes were requested to develop further the general accounting framework within which financial statements may be prepared.

IV. PROBLEMS TO BE RESOLVED

8. The main problem to be addressed in developing a set of accounting standards for application in the United Nations system is the need to devise an appropriate framework for the standards. In this connection, the Panel notes that a set of international accounting standards already exists. These have been issued by the International Accounting Standards Committee (IASC). The objectives of IASC are:

(a) To formulate and publish in the public interest accounting standards to be observed in the presentation of financial statements and to promote their world-wide acceptance and observance;

(b) To work generally for the improvement and harmonization of regulations, accounting standards and procedures relating to the presentation of financial statements.

9. There are, of course, many reasons why standards developed specifically for application to the needs of businesses and commercial accounting cannot be read across for direct application in the very different circumstances of the United Nations organizations. The existing commercial standards are based on a fundamental concept of full accruals accounting, whereas United Nations accounting is a mixture of receipts and payments and income and expenditure, and covers a significantly different range of activities of a non-commercial nature. More generally, the aims and objectives of United Nations organizations, the appropriate disclosure requirements, the interests and needs of the organizations preparing the financial statements and of the various users of the final accounts are in many respects significantly different from those appropriate to commercial bodies.

10. In view of these different circumstances and requirements, the Panel concludes that, while the existing commercial standards may be a useful source of background material, it would be both appropriate and necessary to develop a body of accounting standards to apply specifically to United Nations organizations.

11. The Panel notes, however, that work has already been carried out by CCAQ (FB) to consider the applicability of the IASC's international accounting standards to the United Nations system. This work was carried out by the Secretariat in response to a question raised by the Panel of External Auditors relating to the development of accounting standards applicable to the United Nations system as a whole. The Secretariat, in March 1986, reported to CCAQ (FB) that 12 out of 23 standards then extant were applicable in the case of the United Nations. Furthermore, at its session in March 1987, CCAQ (FB) reviewed the documentation used by the United Nations for the study, which had been prepared by the Inter-American Accounting Association Committee on Standards for the Public Sector, and concluded that the documentation was useful, but the Committee did not feel that other coordinated measures were called for at that time. No further work on this matter has been undertaken by CCAQ (FB).

12. The Panel now believes that the time has come for the administrations of the United Nations system to develop common accounting standards applicable to the United Nations as a whole for the reasons set out in paragraphs 6 and 7 above. In making this recommendation, the Panel has taken note of the growing need for Member States, in the current period of financial constraints, to be presented with accounts drawn up on a common basis in all material respects. The Panel has also noted the United Nations initiatives to encourage the development of accounting practices and techniques in Member States aimed at providing assurance to donors on the use of funds and considers that it would be appropriate for the United Nations to set an example of excellence in this area.

V. FEASIBILITY

13. In the light of the above considerations, the Panel believes that the development of United Nations accounting standards is a feasible proposition. As reported to CCAQ (FB), the United Nations has considered that certain of the international accounting standards of the IASC are applicable to the United Nations system and could therefore be used as a base for the development of United Nations accounting standards.

14. The Panel recognizes that it will be necessary to make use of an expert with terms of reference to develop a set of common accounting standards based, wherever possible, on the standards of IASC and the Accounting Standard Committee of the International Organization of Supreme Audit Institutions (INTOSAI), amended as appropriate to suit the United Nations system. There will also be a need to provide the necessary financial resources to undertake this project.

15. The expert would need to work closely with the administrations and in coordination and cooperation with the External Auditors of the United Nations organizations to ensure that all views and needs are taken into consideration.

16. The Panel is aware that the application of common accounting standards may require some changes to the financial regulations of the organizations, but this should not be an obstacle to the development of more appropriate and consistent accounting standards within the United Nations system.

17. The Panel's experience in adapting the International Federation of Accountants International Audit Guidelines to its own work suggests that it is feasible to use guidelines and standards developed for the commercial sector as a base for those required in the United Nations system.

VI. CONCLUSION

18. On grounds of principle and practice, therefore, the Panel believes that there is a need for the administrations of the United Nations organizations and programmes to develop appropriate accounting standards for consistent application across the United Nations organizations. Due recognition would, of course, in practice be given to any significant differences in the circumstances of the individual organizations concerned.

ANNEX I

Presentation to the Consultative Committee on Administrative Questions (Financial and Budgetary Questions) at its seventy-fifth session

September 1991

I. INTRODUCTION

1. The present annex develops the work already done by the Panel of External Auditors on the need for common accounting standards in the United Nations system.

2. First, the annex briefly summarizes, in paragraphs 5 to 8, the Panel's previous (March 1991) discussions with the Consultative Committee on Administrative Questions (Financial and Budgetary Questions) (CCAQ (FB)) and also draws attention to the discussions which resulted from the Panel's presentation to the Advisory Committee on Administrative and Budgetary Questions (ACABQ) in April 1991.

3. The annex then sets out, in paragraphs 9 to 19, the need for common accounting standards and the reasons for developing them, focusing on the benefits which the Panel feels would result by the application of several International Accounting Standards to United Nations organizations. Annex II outlines those benefits in more detail.

4. Taking account of the above, the present annex concludes by identifying the subject areas that a more detailed study would need to consider. These proposals, which the Panel sees as the way forward in the development of common accounting standards, are included in paragraphs 20 to 22 below.

II. DISCUSSIONS AND PROPOSALS BY THE CONSULTATIVE COMMITTEE ON ADMINISTRATIVE QUESTIONS (FINANCIAL AND BUDGETARY QUESTIONS)

5. CCAQ (FB) considered this issue at its meeting in March 1991. Attention was drawn to the work already done by CCAQ (FB) on the basis of certain international accounting standards, now included in section 17.2 of the CCAQ Handbook.

6. Against the background of the Committee's past work on the subject, CCAQ (FB) posed a number of questions about the need for developing further common accounting standards. Thus, the Panel was asked to provide an elaboration of its proposal for consideration at the seventy-fifth session of CCAQ (FB) in September 1991.

III. PRESENTATION TO THE ADVISORY COMMITTEE ON ADMINISTRATIVE AND BUDGETARY QUESTIONS

7. The Chairman of the Panel of External Auditors presented the interim study to ACABQ in April 1991. As a result of the discussions with the Advisory Committee, it was agreed that the Panel would expand on the work already completed on the applicability of certain standards to the United Nations system (annex II), for submission to the General Assembly at its forty-sixth session in 1991.

IV. ACTION TAKEN BY THE PANEL

8. The present annex and annex II present the action taken by the Panel as a result of the discussions with CCAQ (FB) and ACABQ.

V. THE NEED FOR COMMON ACCOUNTING STANDARDS

9. The original terms of reference set by the General Assembly for the interim study were:

> "To submit to the General Assembly at its forty-sixth session, through the administrative Committee on Coordination and the Advisory Committee on Administrative and Budgetary Questions, an interim study on concrete issues to be resolved through the development of appropriate accounting principles and standards for consistent application in the United Nations System".

10. In the first section of the interim study, the Panel considered the need for common accounting standards. Two key reasons were cited:

(a) Difficulty of comparison between organizations: The Panel felt that the absence of common accounting standards had led to inconsistent accounting treatment of material transactions in the financial statements of United Nations organizations. This meant that comparison between organizations was difficult because the financial statements of each agency might be prepared on a different basis. In these circumstances, the accounts could not easily be compared by Member States or by donors of extrabudgetary funds.

(b) Consistency of external audit reports: The Panel is concerned about the problems that the absence of common standards has caused for External Auditors and, in particular, the difficulty in reporting fairly the financial position to Member States. Within the United Nations system, most organizations have a number of activities that are executed by another United Nations agency. Where this occurs, the External Auditor of the funding organization must rely on the audit carried out by the External Auditor of the recipient organization or executing agency. However, the transactions between these two entities are not necessarily accounted for on the same basis, because each organization may apply its own accounting standards. Experience

has shown that in this situation disagreements have occurred between External Auditors because there is no common basis of accounting. This in turn has meant that what is reported to Member States by the External Auditor on the financial statements of the funding organization is not always consistent with the External Auditor's report on the financial statements of the executing agency, where these interorganization transactions are concerned.

VI. THE BENEFITS OF COMMON ACCOUNTING STANDARDS

11. The second part of the interim study deals with the benefits of common accounting standards. These are presented, to some extent, from the External Auditor's viewpoint. However, the benefits derived from the application of common accounting standards are much wider.

12. The Panel has identified five main benefits:

(a) Ease of understanding: Common accounting standards ensure that the financial statements are presented in a form that is understandable to the reader. This means that financial statements are presented in a common language (using common terms) and that the form of the accounts follow a recognizable pattern.

(b) Relevant information: Common standards ensure that the financial statements present only that information which is relevant to the users, because all accounting standards are developed with the needs of the users in mind. It should be noted that the huge volume of data provided to Member States in financial statements does not necessarily add to understanding. Some of it is not relevant to the financial position as a whole.

(c) Fair presentation: Common accounting standards also ensure that all material transactions, that is those which are likely to impact on decision-making, are reported in the financial statements. This means that the financial statements always present a fair picture of the financial position.

(d) Reliable information: Common accounting standards ensure that all financial statements present reliable information, which is not biased; this means that readers of the financial statements are not misled in any way.

(e) Consistent accounting concepts: Common accounting standards ensure that all financial statements are prepared on the same basis, in particular following the concepts of consistency and prudence. For example, under the prudence concept, all potential liabilities would be recognized. Such liabilities might include the cost of winding down operations and incurring staff redundancies in so doing.

13. The main theme emerging from these benefits is that common accounting standards provide a framework for users (Member States and donors of extrabudgetary funds) to interpret the financial statements.

14. Where extrabudgetary fund donors are concerned, the United Nations organizations should perhaps recognize that potential donors might wish to compare the financial statements of United Nations agencies with similar charities or relief organizations before they make their "investment" decisions. In these circumstances, the United Nations bodies may not compare well if their financial statements are not as easily understood as those of the "private" sector organizations.

VII. THE RELEVANCE OF INTERNATIONAL ACCOUNTING STANDARDS

15. The Panel recognizes that common standards have already been developed for the commercial/private sector, namely, those of IASC. The Panel also acknowledges that some of these standards are not relevant to the United Nations environment. However, there are a number of key standards that provide fundamental guidance on best practice which the Panel feels could be adapted to the United Nations context.

16. The Panel has established that all the United Nations organizations apply some of the standards and that gradual progress has been made towards improving the presentation of financial statements, often with the cooperation and assistance of the External Auditor.

17. The Panel now proposes the development of common accounting standards that, while recognizing current best practice, address the specific user needs of Member States and donors of extrabudgetary funds.

VIII. SPECIFIC AREAS FOR IMPROVEMENT

18. The most visible impact of applying common accounting standards is that they improve the presentation of the financial statements. For the users, this is the most important feature of standards. The interim study presents three examples where the Panel feels that presentation in the financial statements could be made more meaningful through the implementation of common standards, namely, member contribution arrears, termination benefits and year-end transactions.

19. In addition to these cases, there are other examples where a common approach could help readers understand better the financial position. These are:

(a) Statement of changes in financial position: This type of statement is designed to show the reader what movements in cash occurred during the period. It gives an indication of the major sources of funds and the major applications, and as such is a useful summary of the operations in the period. Many United Nations organizations do not prepare a statement of this type; where it is produced it is not always in a form that can be followed easily. For example, some statements contain too much detail, obscuring the purpose of presenting in summary the movements in the period.

(b) Cash balances: In the current economic climate, in which some United Nations organizations are facing a cash crisis, it is important that the amounts disclosed in the balance sheet under "cash" clearly show amounts on long-term deposit, amounts immediately available and amounts held in non-convertible currencies. If this type of information is not clearly disclosed, then a false position of the cash holdings may be conveyed to the reader. However, the Panel accepts that in some cases other information may be given to the Member States at governing body meetings. In these instances, we should be concerned that the cash position is consistent in both the audited statements and any other information made available.

(c) Trust funds: There is a high degree of variety in the way in which trust funds are disclosed in the financial statements. In many cases, a cash basis of disclosure may be used, in contrast to the accrual basis applied to the regular budget. This makes analysis by programme difficult because the two sources cannot easily be combined.

IX. THE WAY FORWARD

20. The Panel has proposed that the United Nations should appoint a consultant to develop a set of accounting standards for common application to the United Nations system.

21. This study would include the following important features:

(a) Ascertaining what the main users of the financial statements (i.e. Member States) want from the statements;

(b) Assessing the extent to which these are met by standards available in the profession;

(c) Ascertaining the extent to which the United Nations currently meets both best practice and the needs of the users;

(d) Developing the common standards based on this information.

22. The consultant should, of course, incorporate into the standards those practices in the United Nations which are better than other alternatives.

ANNEX II

Applicability of common accounting standards to the United Nations

I. INTRODUCTION

1. The International Accounting Standards Committee (IASC) has currently produced around 29 international accounting standards (IAS) for use in the commercial sector. In 1986, the Consultative Committee on Administrative Questions (Financial and Budgetary Questions) (CCAQ (FB)) carried out a review of the standards and concluded that 12 were relevant to the United Nations. At the time of the CCAQ (FB) review, there were around 23 published standards, some of which have now been replaced by new guidance. The Panel has reviewed the current range of 29 standards and believes that 12 could be applied to the United Nations system with little amendment to their current form.

2. All of the 12 standards identified by the Panel as relevant to the United Nations system are cited below, with practical examples given to indicate how each could be applied.

3. The Panel has recognized that the audited financial statements are not the only source of financial information submitted to governing bodies. However, any other information provided to Member States that might report the progress on a particular project/programme or show the status of a particular fund is seen by the governing bodies outside the context of the audited financial statements. While such "other information" might give a useful picture on a particular aspect of operations, the true relationship between such information and the financial position as a whole can only be viewed in the audited financial statements. In view of the wealth of other financial information available to Member States, in the Panel's opinion it is important that the audited financial statements are prepared in accordance with common accounting standards. This will ensure that the "other financial information" is shown in its proper context.

II. INTERNATIONAL ACCOUNTING STANDARDS

A. International accounting standard 1: Disclosure of accounting policies

4. Most United Nations organizations produce accounting policies that meet the disclosure requirements of IAS 1, except that some organizations do not produce prior year figures. Generally, there has been improvement in recent years with better "compliance" in the following respects: all material policies are disclosed and material or fundamental changes in policy are explained.

5. Some auditors have encouraged their clients to disclose the fact that their accounting policies have been prepared in accordance with the disclosure

requirements of IAS 1 (in so far as it is applicable to the operations of the organization).

B. International accounting standard 5: Information to be disclosed in financial statements

6. Most United Nations organizations fulfil the disclosure requirements of the Standard (though the form of account does not necessarily follow the recommended order) with the exception of: disclosure of certain long-term liabilities; disclosure of cash by type of holding; and disclosure of income from investment interest.

C. International accounting standard 7: Statement of changes in financial position

7. Few organizations produce this statement in a form that could be said to comply with the standard. In many cases, too much data is presented without actually informing the reader in the manner intended, i.e. "to improve the understanding of the operations and activities in the period".

D. International accounting standard 8: Unusual and prior items and changes in accounting policy

8. More than most organizations, the United Nations system is subject to "unusual", extraordinary and exceptional events. War, famine and natural disasters figure among the more dramatic examples. In many cases, these events are not disclosed in the financial statements in a manner consistent with the standard. This means that the impact of the events on normal activities may not be clear.

9. Changes in accounting policy are more frequently disclosed, partly through External Auditor interest in ensuring application of IAS 1.

E. International accounting standard 10: Contingencies and post-balance sheet events

10. Contingencies and post-balance sheet events are a rare occurrence in the United Nations system, but there are examples where the Standard might be applicable. One such example is the clearance of the year-end transactions account. Because of the wide geographical spread of United Nations operations, expenditure at the period end may not be fully charged to the income and expenditure accounts for all locations. In these circumstances, expenditure is placed in a suspense account, to be cleared in the subsequent period when imprest returns, and so on, are received. Information from this clearance process might have a significant impact on the financial statements and so should be reported in accordance with the IAS.

F. International accounting standard 13: Presentation of current assets/liabilities

11. Application of this standard is in parallel with IAS 5.

G. International accounting standard 14: Reporting by segment and international accounting standard 27: Consolidated financial statements

12. Few United Nations organizations implement the requirements of IAS 14 in full, but appropriate application of this standard could provide important information to the user of the financial statements, such as statements of income and expenditure by programme or statements of income and expenditure by geographical region.

13. Many United Nations organizations present their budgets to the governing bodies by programme or by geographical region, but few give the outturn information that would allow for comparison. Implementation of IAS 14 would ensure that this information is provided.

14. Similarly, IAS 27 states that consolidated financial statements should be presented using uniform accounting policies, including a common accounting basis.

H. International accounting standard 11: Accounting for construction costs

15. Although this standard relates primarily to the financial statements of contractors, it lays down important principles that could equally be applied to construction projects under way in United Nations organizations.

16. It states that construction costs should be calculated in one of two ways:

(a) The percentage completion method (by which costs are determined by reference to the stage of completion of the contract activity at the end of each accounting period); or

(b) The completed contract method (by which costs are only determined once the construction work is completed).

17. At present, neither method is specifically followed by United Nations organizations. Although partially completed projects are valued on the assets and liabilities statements, the method of valuation is not disclosed.

18. A common standard on the valuation of construction costs would ensure consistency and comparability between financial statements in this significant area.

I. International accounting standard 19: Accounting for retirement benefits

19. This standard requires that the cost of retirement benefits should be determined using an approved actuarial method consistently applied and disclosed in the accounts. This requirement is not generally applied by United Nations organizations.

20. The advantage of introducing a common standard on this topic would be to ensure that each organization discloses all contingent liabilities fully, having followed a universally acceptable method of valuing the liability. Such a practice would be in accordance with the fundamental accounting principle of prudence.

J. International accounting standard 20: Accounting for government grants

21. This standard states that grant income should be recorded on an accrual basis, so that in the income and expenditure account, income is matched with the related expenditure the grants are intended to fund. At present, many United Nations organizations apply a combination of cash and accrual accounting policies. For example, some record income on a cash basis, while expenditure is on an accrual basis.

22. A common standard on the use of accrual accounting would greatly enhance the comparability of financial statements relating to United Nations organizations, both with each other and with similar organizations outside the United Nations.

23. It would also be in line with the policy laid down in the CCAQ Handbook (section 17.2, para. 5(a)), which lists accrual as one of the fundamental accounting assumptions. It also emphasizes the importance of consistency, which cannot be achieved within a set of financial statements if a combination of accrual and cash accounting policies is applied.

K. International accounting standard 25: Accounting for investments

24. This standard requires a distinction between long-term and current investments, whether or not such a distinction is made for assets as a whole.

25. Many United Nations organizations do not make this distinction; instead, deposits and securities are usually shown as a single figure. A distinction between those investments which could be realized immediately and others which are not so liquid is important for the users of the financial statements who may be concerned with the short-term cash position of the organization.